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DEFENSE SPENDING COMMITMENTS

HEARING

BEFORE A

SUBCOMMITTEE OF THE

COMMITTEE ON APPROPRIATIONS
UNITED STATES SENATE

NINETY-EIGHTH CONGRESS

FIRST SESSION

SPECIAL HEARING

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DEFENSE SPENDING COMMITMENTS

FRIDAY, DECEMBER 2, 1983

U.S. SENATE,
SUBCOMMITTEE ON DEFENSE,
COMMITTEE ON APPROPRIATIONS,
Washington, D.C.

The subcommittee met at 9:45 a.m., in room SD-192, Dirksen Senate Office Building, Hon. Ted Stevens (chairman) presiding.

Present: Senator Stevens.

DEPARTMENT OF DEFENSE

DEPUTY SECRETARY OF DEFENSE

STATEMENT OF HON. PAUL THAYER, DEPUTY SECRETARY OF DEFENSE

OUTYEAR SPENDING COMMITMENTS

OPENING STATEMENT OF SENATOR STEVENS

Senator STEVENS. Good morning, Mr. Secretary.

This is the time we have scheduled for testimony from the Department on future spending requirements for growth and modernization investments in military weapon systems.

Let me state that we had this hearing scheduled for earlier in the week, but at the request of some of the members who are now out of town—I don't know how many are going to appear this morning—it was rescheduled by mutual agreement for this morning.

PROCUREMENT COST INCREASES

Military procurement appropriations have risen sharply since 1980, from less than $40 billion to probably more than $100 billion in fiscal year 1985. In other words, we are in the process of tripling our military hardware investment for the first half of this decade. Many of us who support this modernization—I am one of those—and the strengthening of our military defense systems also now have growing concern over the largely uncontrolled spending commitment that results from this kind of investment growth.

ACTUAL DOLLAR OUTLAYS

Actual dollar outlays, the spending that directly affects the budget deficit will also rise sharply in the next few years to pay off these investments. The two aircraft carriers that we funded last

year are an example. There has been no significant outlay resulting from that commitment. Yet, so much of the $6.5 billion will have to be spent over the next 3 to 4 years, that spending now is uncontrollable.

NEW SYSTEM COSTS

The expensive new systems we are producing in greater numbers—tanks, airplanes, ships, missiles—all require people to operate them and maintain them. They all require spare parts and periodic overhaul. They all need extensive support systems, including training, to keep them functioning. These operation and support costs are also largely uncontrollable if we are to keep all of these weapon systems deployed and ready for whatever the military requirements are.

The purpose of this hearing is to focus on these outyear spending requirements to determine just how manageable they are within the context of the ever-increasing defense budget. We need to better understand any future impact of the production decisions we are making today so we can gear those decisions to the affordable limits of future budgets. I made such a commitment to hold such a hearing at the time I got the support from my colleagues to get this last appropriations bill through the Senate.

EXPANSION OF WEAPONS PRODUCTION

The Department continually presses for expanded weapons production as evidenced by the sharp rise in procurement rates. Congress also demands production increases even beyond the budgeted levels. The most recent example of the increases Congress approved and demanded are the F-16 fighters and M-1 tank production, which go beyond the department's attempt to maintain those two programs at a steady production rate.

So we are not trying to point the finger at you or at the Department today in this hearing. We want to ask questions and start developing a record. We are trying to find out where we are headed, and we need to know more clearly the impact of all those production decisions. We need to send the word to our own colleagues in the Congress that add-ons on this bill in the future are out of the question.

PERSONNEL REQUIREMENTS

A major part of these after-costs is related to personnel. We will need more and better trained military personnel, and we looked into the rising cost of this personnel at a hearing earlier this week. Later, probably in the early part of the next session, the committee intends to look more deeply into the outyear impact of our global commitments, another force that is driving the defense budget.

Today we will concentrate on procurement-related issues, and their closely associated operation and support costs. We also want to try to examine the growing trend in Congress, and perhaps in the administration, to consider the defense bill as a jobs bill. Too often I fear, as I have repeatedly stated, weapon production deci-

sions rely too heavily on the economic benefits that accrue to particular communities where the systems are produced.

INTRODUCTION OF WITNESS

We are happy that you have taken the time to come today, Mr. Deputy Secretary of Defense. We are most pleased that you are willing to take the time to discuss this. It looks like this is going to be a discussion between you and me, but it will be more than that because it is going to be a discussion in public about where we are going and about the problem that we have got to solve to get there.

You and your predecessor have been responsible for achieving significant savings during this period of rapidly increasing spending to support rebuilding of our military defenses. Your initiatives such as multiyear procurements, economical production rates and increased competition have brought about significant savings in many of these weapon systems.

In fact, many of the budget reductions that our committee was able to recommend this year were based upon actual savings that we ascertained in our review of your request with your staff, as a result of the procurement initiatives that you have instituted. I think the public should know that you have done a tremendous job.

The news is not always bad. On that upbeat note, hope that you will understand that I truly welcome you before the committee today. Your full statement will be printed in the record. We will be happy to know if you have anyone along with you that you would like to identify for the record.

With that, I would ask that you proceed with your statement. I am pleased that we do have this opportunity to clear up some of the misconceptions appearing in the press at the present time concerning the meeting that took place earlier this week, which will come out later, I think.

It is nice to see you here, Mr. Secretary.

MODERNIZATION OF MILITARY FORCES

Mr. THAYER. Thank you, Mr. Chairman.

Let me say that I am pleased to be here also. I would like to take the opportunity in appearing before you today to address some of these concerns that you expressed about the long-term effects on the defense spending implied by our current efforts to restore and expand our military forces. You are not alone in your concern over whether we can, as a Nation, afford an increasing level of defense funding commitments. These concerns focus upon not only the financial effects of high future levels of outlays upon Federal deficits but also upon industry's ability to support the demands of our defense requirements.

Since the earliest days of this administration, all planning associated with our determination to modernize our military forces and assure adequate levels of readiness has incorporated outyear spending projections. The question of affordability has been carefully examined and is an integral part of our annual program budget review. As a matter of fact, it is gone on constantly. For those who may be concerned about the large dollar figure associated with de-

fense spending, I think it is important that we place our defense costs in what I consider to be the proper perspective.

DEFENSE BUDGET

One consideration is the current and future share of the national income allocated to defense. During the period fiscal year 1981 through fiscal year 1989, the defense share of the gross national product is projected to grow from 5.4 percent to 7.5 percent—actually, I think it will be a little less than that. This growth will still result in lower percentages of GNP allocated to defense than in previous years. The same is true for the defense share of the total Federal outlays. We may be addressing larger defense totals but, at the same time, I think we must admit that our share of national resources still remains in a relative sense moderate.

INDUSTRIAL CAPACITY

In addition to financial implications, there is the question of industrial capacity and whether our Nation can absorb and satisfy the increased demands of our defense requirements. We have looked very carefully at this issue and recent independent studies indicate that even with the industrial capacity utilization now approaching the 80-percent level, the economy is more than adequately accommodating our defense needs. Further, we work closely with industry representatives in order that they are aware of and prepared for defense business and have sufficient time to achieve the necessary capital investments and meet labor requirements.

We also work very carefully to achieve a proper balance of resource utilization within the defense budget itself. Here I am referring to investment-related requirements as contrasted to operational requirements, broadly classified as readiness. Our budget projections incorporate the outyear costs associated with supporting and operating the weapon systems being produced today.

CONTROLS ON DEFENSE SPENDING

Finally, there is concern that the outyear outlays of our current defense buildup will exacerbate the projected Federal deficit. There are those who feel that reductions in defense are primary means of controlling these deficits. It is important to recognize from the start that we have made significant efforts to control defense spending. We originally anticipated an increase in defense spending over projections of the previous administration for fiscal year 1982 through fiscal year 1986 of $116 billion. To date, as a result of reductions and economies of operations achieved within the Department as well as congressional actions, the spending increase has been reduced by over $79 billion, almost $80 billion. This has been a significant contribution in my opinion to sound fiscal policy.

Because much of the relatively small portion of Federal outlays that are considered controllable is defense related, reductions to defense requirements are often viewed as the most expeditious means of reducing the Federal deficit. For those who may agree with this philosophy, let us remember the realities of our defense needs and commitments today.

In an era when the threat to our national interests and security are ever growing and expanding worldwide, we have seen our national investment in defense neglected all through the 1970's. While this administration's commitment to restoring and modernizing our military forces remains strong, we have made every attempt to achieve the mandatory growth within the context of fiscal control. We feel that the future security of our social and political institutions in the final analysis must determine the affordability of our defense program.

Thank you, Mr. Chairman. I would like to try to answer any questions that you may have.

[The prepared statement of Mr. Thayer follows:]

STATEMENT OF HON. PAUL THAYER

Deputy Secretary of Defense

Before The

Senate Subcommittee on Defense Appropriations

December 2, 1983

Mr. Chairman, I am pleased to appear before your Committee this morning to discuss the effect on future spending requirements resulting from the current buildup of our Nation's military capability. These defense funding commitments have led some to ask, as you have recently noted, whether we can afford this buildup. Since the inception of this Administration, we have looked carefully at that question, and we will continue to do so. Based on our analysis I believe we can accomplish this buildup without serious risk of financial or economic disruption.

The Question of Affordability

The affordability of this buildup can be analyzed in different ways. One perspective that is often discussed and has been described by Secretary Weinberger and others in this Administration is the current and future share of the national income devoted to defense. In FY 1981, the total defense budget counted for about 5.4 percent of our Gross National Product (GNP). Today, in FY 1984, the defense share of GNP will be about 6.5 percent. By FY 1988 and FY 1989, the figure should be around 7.5 percent. If we evaluate affordability for defense as a share of our national income, and compare what has taken place and is likely to take place throughout the rest of the 1980's with previous periods, as the first chart does, we will continue to allocate economic resources to defense on a rather modest scale compared to past practice. Defense as a share of the total federal budget shows a similar pattern. The next two charts provide a complete time series analysis describing these trends for the years FY 1960 to FY 1988.

This is one way of looking at affordability. There are others, of course. For example, there has been considerable interest in how this defense buildup will affect certain industrial sectors in our economy. In 1982, the Department of Commerce (Bureau of Industrial Economics) finished a study of the sectoral impact of the proposed defense buildup which focused on whether our military revitalization could be achieved without creating inflationary pressures and supply shortages (so-called "bottlenecks"). This in-depth analysis, undertaken with our full cooperation and under the guidance of the Cabinet Council on Economic Affairs, concluded that existing domestic capacity is adequate in most cases and will remain adequate to supply projected defense and nondefense needs.

Certainly, a contributing factor to these results was the fact that the study was undertaken during the early phases of recovery from recession when capacity utilization in many industries was below 70 percent. However, reviews undertaken since that time by private forecastors such as Data Resources, Incorporated (DRI), indicate that even with the current strong pace of the recovery, U.S. production capacities will remain generally adequate to meet future required defense demands. In fact, the

latest reports show that even with capacity utilization rates for our manufacturing industries approaching the 80 percent level, the economy is more than adequately accommodating defense needs.

Moreover, unlike previous periods of increased demand for defense goods and services, we have made some institutional changes in the acquisition process, and regularly evaluate the industrial requirements resulting from future demands. For example, we work closely with industry representatives to provide them with the necessary information so that they can better prepare for defense business and pursue the necessary capital investment and labor requirements on an efficient schedule.

Another aspect we have watched carefully in terms of affordability is the balance of resources within the defense budget itself, especially between recent increases in investment-related budget authority as contrasted to the operating portion of our budget, usually broadly categorized as readiness. The question we are often asked is: Can we afford this emphasis on the investment portion of the defense budget without causing a future shortfall in the operating accounts?

It is, of course, difficult for anyone to say exactly which future operational needs will be associated with each dollar added for investment. But, we do account for the phase-in of new weapon systems, the phase-out of older weapon systems, and the related changes in support requirements. While there may be uncertainty about the exact number and timing of weapon system introductions and inactivations and their respective financial impact by fiscal year, enough data are available to provide reasonable confidence that programed force levels can be supported within the total amounts programed. These estimates are updated and refined each year. The fourth chart enclosed will give you some dollar comparison of these trends adjusted for the effects of inflation.

It should also be noted, in making judgments on the balance between investment and operating accounts, that a significant portion of the procurement title does not represent solely investment in new or expanded weapon systems but rather the support of weapon systems previously bought. Even though these amounts are appropriated and spent as procurement dollars, they are really operational and readiness programs. For example, the procurement title includes funding for spare parts and support equipment which should be viewed in the same context as the operating accounts when evaluating the balance between investment and operations.

Effect of the Deficit

Today we face the prospect of much larger federal deficits than we have experienced in the past. As a result, the rate at which federal spending grows in the future is of obvious concern to both the Administration and the Congress. When this is considered along with the increases in the Defense budget that have been requested and appropriated since FY 1981, there is concern that these obligations will spend out in the next few years at just the time that we may need even further fiscal constraint to lower federal deficits.

What I do not believe is fully recognized is that, since the fall of 1981, defense spending has already been cut back significantly. The original defense buildup plan for defense was estimated to add $116 billion in outlays for the years FY 1982 to

FY 1986 over the total estimated by the previous Administration. To date over $79 billion of that outlay increment has been removed through a series of reductions and economies of operations, as well as the action of the Congress. This does not translate into a reduction in the federal deficit by an equivalent amount because reduced defense spending lowers tax payments from the private sector which, in turn, lowers federal receipts; but, nevertheless, it is a significant contribution to a sound fiscal policy. We are looking at a different spending picture for defense today than we were three years ago, as chart number five indicates.

Another aspect the Chairman has recently noted that is important to the fiscal equation today is the relative controllability of federal spending, and more particularly defense spending. According to data provided in the FY 1984 budget, over three quarters of total federal spending is defined as relatively uncontrollable under present law -- including programs such as social security, unemployment assistance, and medical care. Of the remaining one quarter of the federal budget that is described as relatively controllable -- primarily because it is subject to annual appropriation -- nearly three-fourths is in the defense budget.

The sixth chart shows this concept in bar chart form. If the budget authority and outlays are added together for all five years, FY 1984 through FY 1988, over that period only about 10 percent of the projected spending will come from FY 1984 and prior, i.e., appropriations that Congress has already made to date. The rest of the spending must yet be derived from congressional approval. This, of course, allows defense programs to be too often viewed an easy vehicle for achieving further funding restraint. We share the common concern over large federal deficits, but we must not continue to seek to reduce deficits at the expense of our military forces.

Recent CIA estimates of a moderation in Soviet defense spending do not negate the fact that over the past 20 years they have undertaken an unprecedented force expansion and modernization effort. It is this buildup and the growing willingness of the Soviets to project their military power that poses the most serious threat to the United States and its allies. Afghanistan, Poland, the Korean Airlines (KAL) incident, and most recently Grenada underscore the continuing and even growing nature of the threat to our security and worldwide stability. Our responsibilities as a leader of the free world require that we allocate a level of defense resources sufficient to ensure that our vital interests, commitments, and responsibilities are met. We believe that the future security of our social and political institutions, in the final analysis, must determine the affordability of our defense program.

Thank you for allowing me to share my thoughts with you today.

Chart 1

DEFENSE SPENDING AS A PERCENT OF GNP AND FEDERAL BUDGET OUTLAYS

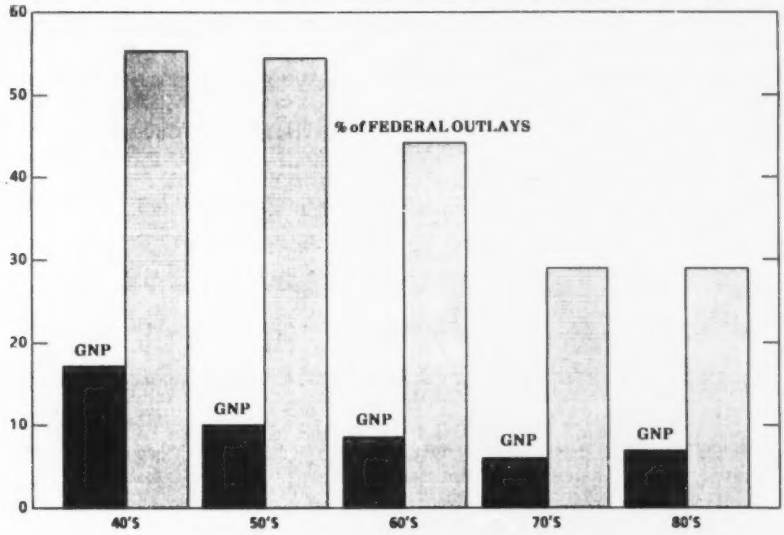


Chart 2

DOD OUTLAYS AS A % OF GNP

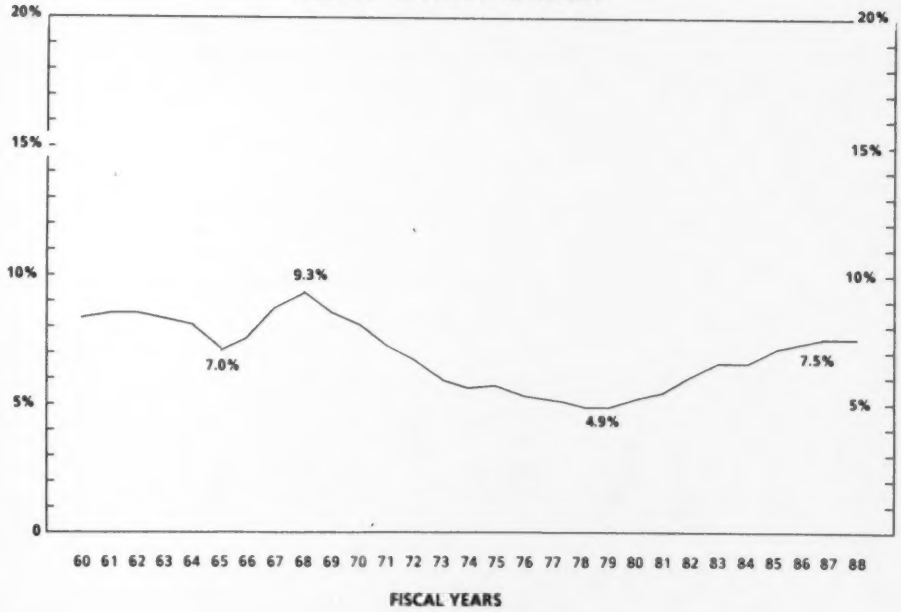


Chart 3

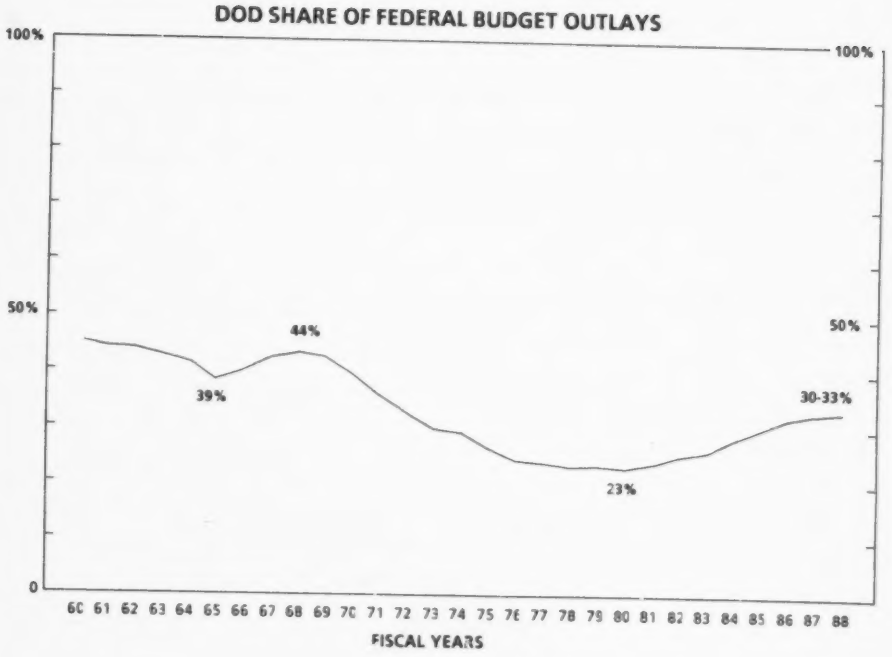


Chart 4

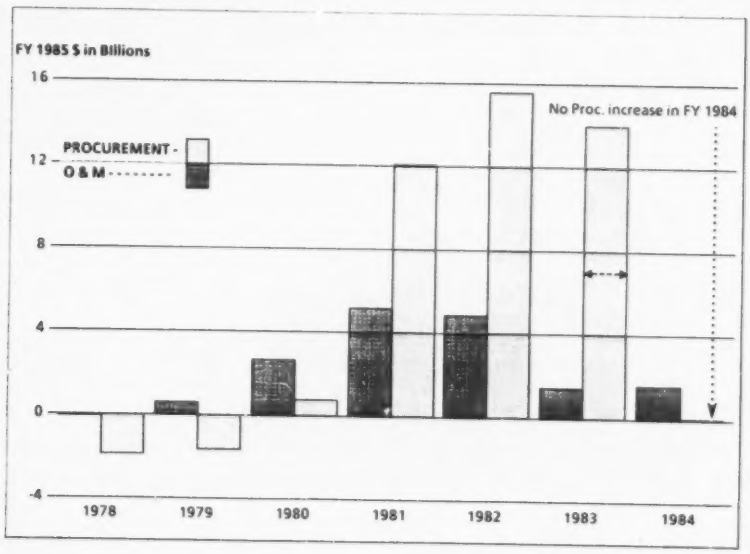


Chart 5

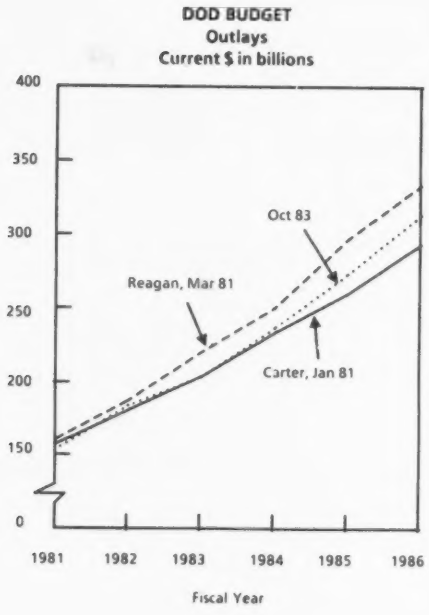
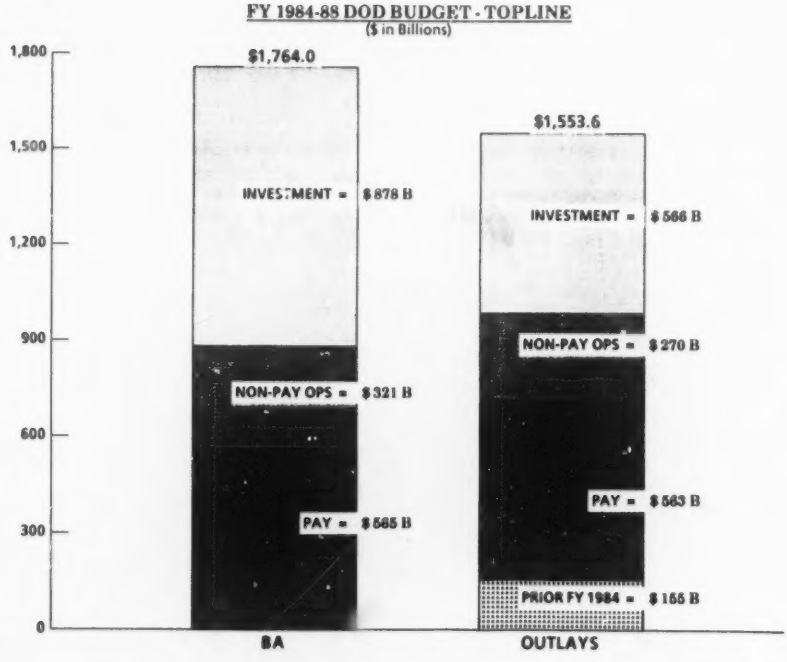


Chart 6



REFERENCE TO STATEMENT CHARTS

Senator STEVENS. Mr. Secretary, I want to thank you. Your complete statement, as I indicated, will be in the record as well as your summary comments.

I find the charts that are attached to your statement very interesting, and we will reproduce them in the record of this hearing also. In particular, the chart that refers to the DOD outlays as a precentage of gross national product over the period of years since 1960 (chart 2) is very revealing, I think, because even at the top of the spending projection, which will occur in 1987 and 1988, the Department's spending will be at approximately the same level as a percentage of the GNP as it was in the 1960's, which was a period of the last part of the Eisenhower administration and the first part of the Kennedy administration. Many people, I think, are not aware of that.

Also, your chart that deals with the DOD's share of the Federal budget outlays (chart 3) indicates that we will probably go up to a 30-to 33-percent level by that same period, 1987 and 1988. This will be less than the period that I mentioned of the sixties. I think they are very enlightening charts, and I will try to make those points as I ask questions.

INFLATION

Mr. Secretary, as a practical matter, most of the reductions that we have been able to take are related to inflation. Isn't the major source of our reductions so far in defense spending from the original 1981 administration projections, the actual savings that have come about because of inflation savings, fuel savings, and various savings brought about by flattening out the curves as far as the recession is concerned?

Mr. THAYER. Inflation has had a favorable effect, but it certainly doesn't account for all of the reductions.

REDUCTIONS

Senator STEVENS. No; some of the reductions, as I have indicated, have come with the initiatives that you have come forth with in your procurement and production decisions. But basically, I think, as we have quantified it in this committee, the reductions that we have been able to make have been associated with fuel savings and with inflation reductions as the principal source.

Mr. THAYER. I don't know what the ratio is, or what the percentage is, Senator. I have just been handed a note that about two-thirds, in our calculation, of the $79 billion that I mentioned earlier as a reduction, have been inflation related.

Senator STEVENS. I think that is significant. I think that it is one of the things that we have to keep in mind that we are really getting a better modernization program for less real dollars as a result of the inflation battle being almost won now.

AIRCRAFT CARRIERS

One real concern now, as I mentioned for instance, are the aircraft carriers. As we look out there in the future, whether or not

they are going to be able to accommodate the commitments that we have already made, that are already authorized. The major battles are over as far as I can see on the major weapon systems—the M–1, the M–X, the aircraft carriers, the submarines, the Bradley vehicles.

The basic systems that are part of the modernization are all authorized, and additional procurement has been brought about by the bill that has just been presented to the President for the 1984 appropriations. This means that those are fixed costs for us as we see them unless you make some decision concerning the staging or the rate of production.

REAL GROWTH FIGURE DEADLINE

What we are now worried about is whether or not we can support those procurement programs within the predictable size of the budget in the outyears. Have you made that comparison of our ability to stay within the guideline of the real growth figures?

Mr. THAYER. Yes, sir. The buildup of unprojected or improperly projected operational requirements in terms of the budget, I agree, has been in the past certainly treated optimistically. It is our firm intent to insure that this is not the case in the scrubbing that we will go through here in the next few weeks with the fiscal year 1985 budget and the projections beyond that.

I am personally very concerned about the importance of projecting realism into all facets of our budget, which I don't think has always been the case in past years, although I believe that in this administration there has been some real progress made in this area, and more importantly it has been institutionalized so that I think it will be a way of life more so in the Department of Defense in the future than it has been in the past. I am speaking still of a realistic budget, and that covers all aspects of the budget.

Readiness per se, I consider to be a blend of all the categories that we are fond of talking about, including modernization, readiness, sustainability, O&M accounts. All of this to me, Mr. Chairman, adds up to readiness, if it is properly balanced.

My concern at least is that we can get to the point in future years where we have a lot of very fine equipment, ship, tanks, and aircraft, because of the realism of the budget ceilings which we will face, and that there will be a squeeze put on the ability to train and maintain a high degree of readiness with that equipment in the modernization program. Let me assure you that I am personally, and Secretary Weinberger is well aware of this pitfall, if you can call it that, if it is overlooked, and we don't intend to do that.

MANPOWER INCREASES

Senator STEVENS. The Congress has rejected for a series of years manpower increases in the Department. That has been one of the considerations that led some of us—I am one of them—to oppose the refloating of the battleships, to oppose increasing production rates on attack submarines, first from one to two, and then two to three, and now it has gotten to four, because of the manpower requirements in the outyears.

Will we be able to provide the manning of the new tanks, ships, submarines, and aircraft carriers, and fighting vehicles without a substantial increase in manpower?

Mr. THAYER. We will have to have some increase in manpower, and I think that this is a basic part of the structure of this President's projected budget starting in fiscal year 1982. We have done, I think, at least a credible job and we can do more in contracting out certain services that have normally in the past required military personnel. I think we can do more of that in order to hold our ceilings within reasonable levels. But, coming back from such a low level, and essentially, as described a few years ago, a hollow army, there is no way to get back to the point of a deterrent posture in our modernization objectives, and readiness objectives.

Senator STEVENS. I remember once this committee was in Europe and we read a story in one of the European papers about one of our naval vessels in Norfolk that couldn't leave the dock because it didn't have a sufficient manpower base to leave.

I think that kind of a report does more to destroy the image of our ability to defend our country than anything else. Yet, we now see that this is going to exceed our projections unless there is some change as far as the policies of the Congress are concerned.

We would have to have large increases in active military strength in order to accommodate these new weapon systems, or there would have to be a change in the policy with regard to the utilization of the Guard and Reserves, which is basically the direction that the Congress is trying to point.

Mr. THAYER. Of course, we have made some big strides in that regard. We have strengthened our Reserves in every way possible. The point should also be made that as these new force units are fielded, the older units that will be freed up to some extent to conserve these manpower increases.

It is not a case of a direct ratio. As the budget goes up in the modernization category, and the fielding of equipment and weapon systems such as GLCM and Pershing, and the carriers that you spoke of, there will be some increases required, but those will not be in a direct relationship to the increases in the budget because there will be older forces that will be freed up and give the manpower to accomplish the new requirements.

I think our manpower projections for the most part, Mr. Chairman, are fairly well controlled and fairly accurate over the foreseeable future, but Congress will have an awful lot to do with controlling that in future budgets because there is, as I said before, available to you, in any programmatic decisions that are made on the hill, the manpower requirements that go along with those programmatic decisions.

CURRENT MANPOWER COSTS

Senator STEVENS. We used to say that about 60 percent out of every defense dollar was for manpower or related costs. Is there a figure now that is accurate, because this is no longer accurate.

Mr. THAYER. It is far below that now. It is closer to 42 or 43 percent.

Senator STEVENS. That is because of the modernization procurement policies that we are pursuing.

Mr. THAYER. Yes. In many cases, modernization does not increase manpower, it reduces it. In a new aircraft, for example, the maintenance man-hours per flight-hour of an F–18 is considerably less than an A–6.

UNIFORMED PERSONNEL INCREASES

Senator STEVENS. That is what we hear, but when we got into the actual hearings last year and we questioned the uniformed personnel, we understood that, in actual numbers, there appears to be an increase in actual numbers because of the type of systems.

You take an engine out of an M–1 and you replace it in the field. Then you have a crew to take the engine that has been taken out to be repaired. Then you have another crew to bring the other one back up. So we actually ended up with an increase in the number of people handling the equipment rather than a decrease.

It is true that on the flightline there are probably less people, but there is more backup for these sophisticated systems than before. It appeared to us that that had not been cranked into the total manpower picture, the maintenance requirements in the handling of these high-tech new systems as far as the manpower requirements were concerned.

Our information was at first that the new systems were not personnel intensive, but as we examined it we learned that they are much more personnel intensive because of the redundancy required in the kind of use of modular replacements in spare parts.

We can't focus on some of those things as far as the outyears are concerned until we can get some greater detail on that, and this is not the day for it. However, we question seriously whether these new systems are not more manpower intensive in the total operation of the military than the systems that they are replacing.

Mr. THAYER. I think that we owe you a better analysis on that than what I am able to give you today. I am not familiar with the particular hearing that you just referred to.

Senator STEVENS. Part of it came from visits in the field where we went and looked at these things. We went to Texas, and we went over to Europe to visit some of them in the field, and we inquired as to how many people were handling the M–60 and how many people were handling the M–1 the engines removed in the field, and what happens to it, and where it is taken for repair. We followed that through in one of our trips and we reached the conclusion that there was going to be more manpower involved in the tanks than we had been led to believe.

Mr. THAYER. Senator, I don't have to tell you, you are well aware, I think, of the state of readiness and the state of the warfighting capability of our Armed Forces a few years ago.

Senator STEVENS. Yes.

Mr. THAYER. One of the main reasons for that was a lack of manpower, a lack of spares, a lack of logistic support, and a lack of what we refer to as operations and maintenance accounting across the board. We didn't have enough of anything to sustain ourselves

for any appreciable length of time in any major conflict, disregarding the readiness factor.

Some of this increase in manpower has got to be plain catchup in the interest of readiness. It is impossible to have a high degree of readiness without an adequate supply of highly qualified people to maintain and operate the equipment, and without the logistic support. So we are coming from a low level of a few years ago, and we are just now reaching the point where we can say—in most areas, now that the pipeline has filled up and the modernization equipment, the readiness commitments that were made, the training and the higher level of qualified talent that is available to us—that we are at this point getting to a degree of readiness which we have been working toward for 3 years. But it has required, as I said, a lot of catching up in all of the areas that I have just mentioned to get to an adequate level from a very low level.

INCREASED ROLE OF GUARD AND RESERVE

Senator STEVENS. Involved in that catching up, is there going to be a recognition of the congressional indication and intent that the Guard and the Reserves play a greater role in readiness?

Mr. THAYER. They already are, and they already have been getting the resources and the attention to accomplish that. It has gone way beyond any lip service or pretending to do it, it is being done.

Senator STEVENS. When we were in Europe, we were briefed as to a $10 billion construction program that was contemplated in a repositioning of our forces in Europe—this isn't the time to go into that. We came back and we had some meetings. Some of the members who weren't even there objected to the extent of the operations that are going on in Europe right now, and insisted that we move a portion of the funds that had been budgeted from active to Reserve and National Guard, which we did. That was in 1982, and we have done that again this year.

I am not sure that it really has become departmental policy to pursue a concept of utilizing even to a greater extent than they have, the Guard and the Reserves in order to maintain the affordability of the systems that are going to be required in the modernization. That was a basic decision of the committee, and we hope that you would explore that concept.

One of the things that we see is that the defense budgets still keep the inflationary rate high as they are presented to us. As I indicated, this year we took substantial reductions on two occasions for inflation savings and fuel savings. Are your assumptions for 1985 and 1986 now going to take into account in their first instance the lowering of inflation in the Nation generally and the fuel savings that are there?

Mr. THAYER. Yes, sir. We have insisted within the administration that we be allowed to deal with realistic inflation numbers and are, in my opinion, doing so. We have, as you know, in connection with the fiscal year 1985 budget, a very tough exercise ahead of us within the next few weeks to present that in final form to the President and, in turn, to Congress. There will be some very tough decisions that have to be made.

Senator STEVENS. This is not the time to inquire into those decisions, but I want to state to you and point out to some people who are here today about the stories in the papers that I don't remember the $305 billion figure being mentioned. I was called to the telephone several times during the meetings. I don't know about that figure, but I do know that there is a feeling that we may see requests come to us for further moneys in 1984 while we are, in fact, trying to work out the 1985 budget. Is that going to happen?

We expect the pay increase, we specifically put that off for the supplemental for 1984 in connection with the appropriations bill. Incidentally, the real growth with that in there is somewhere around 3.4 percent in terms of the final bill, if we put the pay increase into the appropriations bill. But beyond that, are we to expect requests for additional funds in the form of program supplementals for 1984?

Mr. THAYER. I have a little difficulty answering that at the moment because we are still going through and reconstructing in the aftermath of the conference committee decisions, and what that did to us in several categories. I think there were over 800 changes made, and it is going to take us another few days or a week in order to really determine where we stand.

RESEARCH AND DEVELOPMENT

Senator STEVENS. One of the stories I saw dealt with the question of R&D. We started off with an authorization conference report that had reduced your R&D request by $1.2 billion, and we took out another $180 million that was related to inflation. As a result, we finally ended with a figure that was $1.8 billion below the budget.

It now appears that we hear rumors, but I think the source was not exactly a rumor source, that we should expect a supplemental dealing with research and development, when the basic cuts in research and development were in an authorization bill, not an appropriation bill, I don't know how we can deal with that on a supplemental.

I just hope that as you examine those items that were reduced from the budget that there is an awareness of the difficulty. Most people don't realize that we will be in session for 120 days next year, with 2 conventions, a Presidential election, and 19 separate primaries. A substantial number of people will be gone because of the election process.

Next year will be a very difficult year to even handle the 1985 budget, let alone put us back to the 1984 mode and looking at those adjustments. One of the things that I would like to urge you to do, if there are problems about the 1984 budget, and the result is to try to accommodate those in the 1985 request.

Mr. THAYER. We may be able to do that.

Senator STEVENS. Even if it went to the figure that they are mentioning, it would be an understandable figure if it really dealt with some of the shortfalls of the 1984 year in my opinion.

Mr. THAYER. I regard that as a very helpful suggestion, Mr. Chairman, and we will certainly look at that in that light very strongly. We may come in with a supplemental, but I think only

where a cut has been made, and where we can come back and clearly show that such a cut is really counterproductive and results in more expense for the program rather than less.

Senator STEVENS. All I would say on those, Mr. Secretary, if they are going to come, I hope that they come separately from the pay increase and the Grenada costs, because I think the pay increase and the Grenada costs are items that ought to be dealt with rather rapidly at the beginning of the next session and should not be controversial.

Mr. THAYER. We would not plan to try to complicate the pay bill or the Grenada costs with an additional supplemental request, because we feel very strongly that those needed to be handled very expeditiously by the Congress.

ADDITIONAL FUNDING FOR 5-YEAR PERIOD

Senator STEVENS. Without gettting into your discussions that are going on about 1985, are you prepared to tell us what kind of additional moneys you need for the balance of the original 5-year period to maintain the modernization program, assuming an optimistic inflation assumption which I think we have to assume, and I hope you assumed, as we approach this next year's budget?

Is there a projection that we can rely on as far as the 1985 and beyond to maintain the ongoing authorization program and the readiness that is contemplated by the 1981 schedule?

What would be the top figure that would be required to do that? The figure for 1984 was $288 billion, and we are now down to $257 billion, assuming that the pay increase is in there.

Mr. THAYER. The DOD budget itself, without the pay increase, is right at $250 billion, slightly less. I can honestly say to you, Mr. Chairman, that I don't have a number from my superiors, Secretary Weinberger and the President, to work to in fiscal year 1985, but I expect to as the Chairman of the Defense Resources Board to have that number of rescrub the 1985 budget work that was done in August, and to come to you in January.

Senator STEVENS. I am not trying to get you to state a specific figure. Let's see if we can go at it this way. The original projection both in 1981 and again in 1983 indicated that the balloon came in 1985. That there really was a rapid increase in real growth in 1985, and it came back down again in 1986 as we started to accommodate the first year of full production of the main weapon systems—as I mentioned before, submarines, aircraft carriers, B–1 bombers, M–1 tanks, and Bradley fighting vehicles, the whole composition of the modernization that is going on. The bulk of the first year's real dollars for production occurs in 1985.

Our worry is that if we are going to continue that, something has got to give, or the production schedule has got to give. Are we in agreement on that?

Mr. THAYER. Something does have to give in fiscal year 1985.

Senator STEVENS. Something has to give or the trendline has to be abruptly changed and look like a very successful corporate chart in 1 year; do you know what I mean. That trendline is going down now, and it would have to go up dramatically. My calculation would be that it would have to be almost 14 percent real growth in

1985 in order to accommodate ongoing production that is authorized and initiated by this year's bill.

Mr. THAYER. We worked initially on the fiscal year 1985 budget based on the projection that was made in the previous year, because we had no better number to work with while the 1984 budget deliberations were going through Congress. If we stayed with our original projections, I agree now that we know what the fiscal year 1984 budget consists of and its top line, we are talking about a very substantial increase. Depending on how one would like to calculate it, it could vary from 18 to over 20 percent. No; we are not going to come back to you with that kind of an increase.

GROWTH OF ONGOING MODERNIZATION PROGRAM

Senator STEVENS. The 1984 congressional budget resolution assumed $297 billion for the defense level for 1985. With the reductions that have taken place in 1984, both by the administration and by the Congress, the question really is: What rate of growth is necessary now to obtain an efficient rate of production in the ongoing modernization program.

Mr. THAYER. The way we had it originally laid out, and since then the front end of the projections starting in 1982–86 were decreased. An attempt has been made, because of what the Department of Defense and the administration evaluate the trend to be, to try and regain some of that in the midyears. At best, there is no way that we see, from a practical point of view, that we are going to meet the original projections. We are not counting on that. We are getting back very close to the projections made by President Carter for the current fiscal years for what that administration felt the budget should be.

Senator STEVENS. Not if you go to constant dollars. The problem with the budget comparisons I have seen is that they are in current dollars. If they are in constant dollars, we are considerably above the Carter projections.

Mr. THAYER. We are at the moment.

INCREASES BY REAL GROWTH

Senator STEVENS. What concerns me, Mr. Secretary, let me put it this way, real growth in 1981 was 12.5 percent, real growth in 1982 was 12 percent, real growth in 1983 was 6.8 percent, and real growth in 1984 is 3.4 percent. In order to accommodate the existing systems that are authorized, are in procurement, and for the bill that will be coming in, we need 13 percent-plus according to our calculations.

Mr. THAYER. We certainly need more than 3.4 percent.

Senator STEVENS. Yes.

Mr. THAYER. Either that, or we delay getting to the objectives that we set for ourselves 3 years ago. In some cases, we may have to delay significantly, and in other cases, we may have to cut vertically as opposed to piecemeal and across the board, and eliminate some programs that we consider to be very desirable.

Senator STEVENS. I have not been too successful in convincing the Senate of the problem of what I call "ante-ing up." I got that from my good friends here on my staff. The increases in M–1, the

increases in the submarine, the increases in production rates have only intensified that problem in 1985. I fear that we will have to now come down in production, and perhaps one of the things that you will have to suggest to us in this revision for 1984 is, in fact, a readjustment of the 1986 production rates to accommodate the fact that those are being produced too rapidly as far as 1985 is concerned.

Mr. THAYER. We expect to eventually get to the levels that we are aiming for in the practical sense. At the moment it appears that that will be delayed from 1 to 2 years.

MAJOR WEAPON SYSTEM PRODUCTION RATE

Senator STEVENS. Do we now have a minimum efficient rate of production for all the major weapon systems that are underway, and can you provide that for the committee?

Mr. THAYER. I can't say that we do.

Senator STEVENS. I think that that is the essential question. If someone could convince me that there is actually a saving, we would have another matter. We didn't see any savings. As a matter of fact, we saw a loss because you are borrowing the money to buy them, and paying an interest rate over the period of time.

We think that we should analyze this now from the point of view of what is the minimum efficient rate of production to meet defense needs. It is not just economics, but it is defense needs. I think that is the thing that you should be able to ask your people to give us when we have our first meetings, and we are going to have our first meetings earlier next year.

Mr. THAYER. I would hope that we could do that, Senator, that we would meet early and come to some fundamental understanding of what our common objectives are, and move the budget process much faster through the Congress than we have been able to in past years, and end up having to contend with a continuing resolution.

Senator STEVENS. In the past, once a weapon system was authorized, to acquire a number of tanks, we then looked at the appropriations process each year to find out how many we could afford each year, and we put up the money. Now we have to wait for the appropriation process to give the numbers that they feel ought to be built under the general authorization program.

Mr. THAYER. One way to avoid a lot of this, of changing production rates and, therefore, costs and destabilizing the acquisition process is through multiyear contracts. I think there are many more programs that are eligible for that kind of treatment.

RETIREMENT POLICY CHANGES

Senator STEVENS. Mr. Secretary, one last question that I wanted to ask you. I know you have another commitment, and I don't want to impose on your courtesy. I am sorry that my colleagues who discussed this hearing with me were here on Tuesday and are not here today.

We now have a change of policy in retirement for the military. We are committed to now fund retirement costs and to pay a portion of the past unfunded liability of retirement costs. As one who

supports this concept of the modernization program, it worries me that part of that budget that is coming in for 1985 must, as I understand, contain those items. We may well find one part of the modernization program squeezed out by an accounting process, which is really an accounting process to earmark moneys in the Treasury. It doesn't produce the dollars. Have your people looked at that process?

Mr. THAYER. I am advised that there is very little increased cost associated with that.

Senator STEVENS. In the first year that may be right. As I understand it, it is going to grow.

The comparison between the military and the civilian pay is aonther matter. I think the day is going to come when those civilians who are working for the Department of Defense their income is going to be so low compared to their military counterparts that there is going to be a morale problem in the civilian section of the Department of Defense. We have to look at the civilian pay costs.

With regard to the retirement concepts, those are now for the first time, as I understand it, going to appear in our bill. As they appear in our bill, they are going to start being identified as part of what the total figure is. I don't care if it is $305 billion, or $287 billion, or some other figure that we think is necessary to get to the concepts of procurement, but if a portion of that is payment for past retirement costs that were not properly funded in past years, it is going to affect our authorization as far as the total figure, because unfortunately we end up by dealing with the total figure.

Mr. THAYER. If you would like, Mr. Chairman, I can provide you our analysis of what this will do not only in the fiscal year 1985 budget, but in the coming years.

OMB FUND TO DEAL WITH UNFUNDED LIABILITIES

Senator STEVENS. What I would like to suggest, because I am chairman of the other subcommittee, too, I think there ought to be an account set up by OMB in the Treasury that deals with unfunded liabilities, and keep them out of the direct program costs of any Department.

Mr. THAYER. We have thought of that.

Senator STEVENS. I think if you could accomplish that result specifically.

Mr. THAYER. All right, sir.

Senator STEVENS. I am informed that I am mistaken, we did not come up with the 13.9 percent. It is a figure that has been derived by a comparison of the past budgets in terms of the projected goals. My staff doesn't want me to be able to get ready to defend where we got the 13.9 percent.

I do appreciate your courtesy in coming. We anticipate a substantial battle next year, Mr. Secretary, if that trendline is any indication to us. I was properly quoted as saying that we would be lucky to maintain the 3-percent level unless we find some special circumstances that would warrant the increase. I happen to think that the special circumstances are there, and I am prepared to present a bill to the Senate to reverse that decline, but I think we are going to have to do it in a way that we all agree on from the very begin-

ning. I am hopeful that the exchange we had will help us have a better working relationship as far as the preparation of that budget is concerned.

Mr. THAYER. I will certainly see that we do our part in that regard.

Senator STEVENS. Thank you very much.

Mr. THAYER. Thank you, sir.

SUBMITTED QUESTIONS

Senator STEVENS. We will have additional questions which we will ask you to answer for the record.

[The following questions were not asked at the hearing, but were submitted to the Department for response subsequent to the hearing:]

ADDITIONAL COMMITTEE QUESTIONS

MILITARY RETIREMENT COSTS

Question. Roughly 5 percent of every defense budget request is committed to military retirement costs. Are there any reforms currently under consideration to curb these costs?

Answer. The 5th Quadrennial Review of Military Compensation (QRMC) has been specifically tasked by the President to review the retirement system in relation to defense requirements and to make recommendations for improvement. All aspects of the retirement system are being addressed as part of this review. This effort is ongoing and the QRMC is expected to complete its work this calendar year.

OPERATING ACCOUNTS

Question. Assuming increasing outlays from prior year commitments will limit options, the only area left to cut current year expenditures is the operating accounts. But the cost to operate and maintain new weapon systems appears to be more expensive than the older inventories. Given this trend, what baseline does the Department use to judge the adequacy of operating budgets?

Answer. We use currently approved budget year estimates as a baseline for the Five-Year Defense Plan, which is developed by the Services at a very detailed (program element) level. These estimates are updated and refined each year. Planned phase-in of new weapon systems, phase-out of older weapon systems, and all of the related changes in support requirements are reflected in these outyear estimates.

It should be noted that a significant portion of the procurement title does not represent solely investment in new or expanded weapon systems, but also the support of weapon systems previously bought. The procurement title funding for spare parts and support equipment should be viewed in the same context as the operating accounts when evaluating the balance between investment and operations.

FLETCHER COMMISSION

Question. Secretary DeLauer testified recently to an estimated $27 billion cost for the Fletcher Commission strategic defense recommendations over the next few years. Do you consider these costs to be additive to the out-year defense program or will something else have to go to make room for the strategic defense program?

Answer. The $27 billion estimate refers to one of the options for the Defense Against Ballistic Missiles (DABM) program which the Administration is currently considering. The specific scope of effort to be undertaken will be determined by the President and submitted to Congress with the fiscal year 1985 budget. A substantial portion of the DABM requirements can be covered within the current DOD budget for DABM-related efforts. As part of the fiscal year 1985 budget deliberations, we are reviewing the extent to which the balance can be accommodated within the outyear defense program.

PROGRAM STRETCH-OUTS

Question. CBO examination of the latest selected acquisition reports found that program stretch-outs for 20 systems forced cost increases of over $5.6 billion. Con-

versely, accelerated production rates resulted in savings of nearly $1 billion for eight major systems. With all the defense funding appropriated in recent years, why are production schedules continuing to stretch out?

Answer. The SAR's address the total development/production period which may exceed ten years. During this time, there are many reasons why a program will change from the original procurement profile; congressional action, revised installation schedule, reduced inventory requirements, changing priorities, revised operational requirements, development slippage, and affordability. Each program is susceptible to these changes and their impact tends to be magnified because of the long time span and fixed baseline program in the SAR's.

CONCLUSION OF HEARINGS

[Whereupon, at 10:45 a.m., Friday, December 2, the hearing was concluded and the subcommittee was recessed to reconvene at the call of the Chair.]

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